

# United Norwest Co-operatives Employees' Pension Fund (“the Fund”)

## Statement of Investment Principles – March 2022

### 1. *Introduction*

TCG Northern Trustees Limited, the Trustee of the United Norwest Co-operatives Employees' Pension Fund (“the Trustee”) has drawn up this Statement of Investment Principles (“the Statement”) to comply with the requirements of the Pensions Act 1995 (“the Act”) and subsequent legislation. The Statement seeks to take into account the principles underlying the Myners Code of Best Practice for pension scheme investment, which has been endorsed by the Government and the Pensions and Lifetime Savings Association. The Statement also seeks to take into account the Investment Governance Group (‘IGG’) principles for defined benefit pension schemes.

The Statement is intended to affirm the investment principles that govern decisions about the Fund’s investments.

The Fund operates for the purpose of providing retirement and death benefits to eligible participants and beneficiaries in a defined benefit framework.

In preparing this Statement, the Trustee has consulted the Fund’s Principal Employer, Co-operative Group Limited (“the Co-op”), to ascertain whether there are any material issues the Trustee should be aware of in agreeing the investment arrangements. However, the ultimate power and responsibility for deciding investment policy lies solely with the Trustee.

The investment responsibilities and powers of the Trustee are governed by the Fund’s Trust Deed and Rules (a copy of which is available for inspection on request) and relevant legislation.

The Trustee has established an Investment Committee to focus on investment matters. While the Trustee retains direct responsibility for setting investment objectives, setting the Fund’s investment strategy and manager structure, it makes these decisions after considering recommendations from the Investment Committee.

The Trustee has also established a Manager Monitoring and Implementation Committee (“MMIC”) (in conjunction with other Co-operative pension schemes) to focus on and review the Fund’s investment managers. The MMIC is an advisory body that may make recommendations to the Investment Committee or Trustee regarding investment manager-related matters.

## **2. *Process for Choosing Investments***

The process for choosing investments is as follows:

- Identify appropriate investment objectives
- Consider the broad level of risk consistent with meeting the objectives set
- Construct a portfolio of investments that is expected to maximise the return (net of all costs) given the Trustee's risk tolerance

The Trustee has adopted a set of investment beliefs, and aims to choose investments and construct a portfolio of investments that is consistent with these beliefs, doing so in a way that takes into account broader environmental, social and corporate governance concerns. Investing responsibly is an important consideration for the Trustee and is covered in more detail in Section 12.

In considering the appropriate investments for the Fund, the Trustee has obtained and considered the written advice of the Investment Adviser, whom the Trustee believes to be suitably qualified to provide such advice. Where matters described in this Statement may affect the Fund's funding policy, input has also been obtained from the Fund Actuary. The advice received and arrangements implemented are, in the Trustee's opinion, consistent with the requirements of Section 36 of the Pensions Act 1995 (as amended).

## **3. *Investment Objectives***

The investment objectives of the Fund are to achieve an overall rate of return that will ensure:

- Sufficient resources are available to meet all liabilities as they fall due;  
and
- Investment returns are maximised at an acceptable level of risk.

The Trustee believes the investment objectives and the resultant investment strategy is consistent with the actuarial valuation methodology and assumptions used by the Fund Actuary.

#### 4. **Risk Management and Measurement**

The Trustee recognises that a number of risks are involved in the investment of the Fund's assets. The Trustee will continue to monitor the key risks, principally:

- **Solvency risk and mismatching risk** - addressed through setting appropriate investment objectives as part of the triennial actuarial valuation taking into account the funding objectives. Mismatching risk is also partially addressed through investing in a Liability Driven Investment ("LDI") portfolio.
- **Manager risk** - addressed through the diversification of the Fund's assets across a range of managers and monitoring of managers.
- **Liquidity risk** - the monthly benefit and expenses outgo is monitored to ensure that sufficient cash balances are available. Investment in illiquid assets is kept to an appropriate level.
- **Currency risk** – addressed through hedging approximately 75% of the Fund's developed overseas currency exposure within equities, and all of the Fund's overseas currency exposure within illiquid and investment grade credit, to Sterling (as far as practically possible).
- **Counterparty risk** – where the Fund enters into derivative transactions, either directly or via pooled funds, these will be collateralised as appropriate. Where possible, the Fund will engage a range of counterparties (with counterparty selection for specific trades delegated to investment managers), with limits placed on exposure to any individual counterparty, to reduce the impact of potential counterparty default.
- **Custody risk** – where assets are held on a segregated basis, addressed by monitoring the custodian's activities and the creditworthiness of the custodian bank, and discussing the performance of the custodian with the investment managers when appropriate. Where custody of the assets is delegated to professional custodians via the use of pooled funds, each manager is responsible for appointing a custodian and monitoring the custodian's activities. The Trustee has considered the risk relating to this.
- **Corporate governance risk** – managed through regular reviews of stock concentration and regular discussions with the investment managers when appropriate. The Fund's equity mandate is split equally between passive and active mandates, each with an ESG focus.

The passive mandate is invested in funds with deliberate 'tilts' towards companies which are assessed by the manager to have better than average "ESG scores". These scores are determined by the manager,

based on several factors / metrics, including several which relate specifically to corporate governance.

The aim of the active mandate is to complement the passive investment and focuses on a long term sustainable approach through active ownership and engagement with the holdings in the mandate. The active equity manager also publishes a detailed engagement report.

- **Sponsor risk** – addressed by regular assessments of the ability and willingness of the Co-op to support the continuation of the Fund and to make good any deficit.
- **Leverage risk** – addressed by regular review of the size, amount and nature of any leveraged investments made by the Fund's investment managers and monitoring of potential collateral requirements (versus an agreed collateral policy).
- **Credit risk** – addressed through holding a diverse range of credit investments across a variety of issuers and sectors, with exposure limits in place, through having in place investment managers who assess the creditworthiness of the debt instruments in which the Fund invests and through appropriate limits on credit quality.
- **Interest Rate and Inflation Risks** – management of the majority of these risks is delegated to the Fund's LDI manager. However, the Trustee regularly reviews a range of liability hedging risks within quarterly reporting discussions (and other analysis from time to time) with professional advisors.
- **Longevity Risks** – the risk of increasing life expectancy of the Fund's pensioners. This risk is not explicitly hedged at present.
- **Environmental, social and governance (“ESG”) risk (including climate change)** – addressed through the incorporation of the Northern Responsible Investment Policy (“RI Policy”) when implementing the Fund's investment strategy, and the annual review of this Policy. This includes engagement with investment managers and the exclusion of specific investments from the Fund's portfolios (where appropriate and viable)

The Fund's passive equity assets are invested in pooled funds which have tilts towards companies assessed by the manager to have positive 'ESG scores', based on a number of factors and reduced exposure to companies with negative ESG scores.

The aim of the active mandate is to complement the passive investment and focuses on long term sustainable approach which integrates ESG at all levels of the investment process. Including through investment analysis, stock selection, active ownership and engagement with the holdings in the mandate.

- All managers are expected to integrate ESG factors into the portfolio construction process and report on their efforts and actions. Bearing in mind the nature of the LDI mandate the integration of ESG factors is focused within the cash fund holding, which includes an ESG screening process alongside other ESG enhancements.

Other risks are addressed within the individual investment manager and custodian agreements.

## **5. Portfolio Construction**

It is the Trustee's policy to consider a full range of asset classes either directly or via pooled funds which utilise a wide range of asset classes and investment management techniques, including but not limited to:

- Equities (UK and overseas, including emerging markets)
- Illiquid Credit
- Investment Grade Credit
- Liability Driven Investments ("LDI")

The Trustee has adopted the following control framework in structuring the Fund's investments:

- There is a role for both active and passive management. Passive management will be used for one of a number of reasons, namely:
  - To diversify risk;
  - To invest in markets deemed efficient and where the scope for active management to add value is limited; and
  - As a temporary home, if so required, pending investment with an active manager.
- Where the Trustee has appointed active managers, the Trustee will regularly monitor performance relative to the benchmark and performance objective via the MMIC and the Investment Committee.
- To help diversify manager specific risk, multiple manager appointments within certain actively managed mandates (e.g. illiquid credit) are preferred where practical.
- At total Fund level and within individual manager appointments, investments should be broadly diversified to ensure there is not a concentration of investment with any one issuer.

- Investment in illiquid investments, such as illiquid credit assets, may be held in limited quantities. The proportion of such investments will be monitored at a total Fund level.
- Investment in derivatives is permitted as agreed on a manager by manager basis as long as they contribute to a reduction in risk or facilitate efficient portfolio management. The use of derivatives and appropriate restrictions in place are considered when selecting and monitoring Fund investments.
- Investment may be made in securities that are not traded on regulated markets. Recognising the risks (in particular liquidity and counterparty exposure), the Trustee will look to ensure that the assets of the Fund are predominantly invested on regulated markets.
- No investment in securities issued by the Fund's Principal Employer or affiliated companies will be made directly (i.e. this excludes any such securities held within a pooled fund in which the Fund invests).
- Borrowing is not permitted except to cover short term liquidity requirements, or as part of a transition to maintain market exposure.
- The Trustee has a policy to consider currency hedging for the Fund's overseas assets. It has agreed, in conjunction with its Investment Adviser, to target a 75% hedge of non-Sterling currency exposure of developed market equities and to target a 100% hedge of non-Sterling currency exposure within the investment grade credit and illiquid credit mandates, where practical.
- For the Fund's segregated investment grade credit mandate, the Trustee has provided the manager with a list of specific investments to exclude from further purchases, where these investments have been identified as conflicting with the key areas of the Trustee's RI Policy.

## **6. *Investment Strategy***

The Trustee recognises that it is not necessarily possible, or even desirable, to select investments that exactly match the liabilities. Given the ongoing commitment of the Co-op to the Fund, a degree of mismatching risk can be accepted on the basis that it is also acceptable to the Co-op and the Trustee is satisfied that the Co-op's covenant strength is adequate to support the mismatching risk.

The Trustee has decided to set an investment strategy, which is expected over the medium term to produce investment returns to meet the investment objectives, while limiting the risk inherent in the mismatch between assets and liabilities to an acceptable level to the Trustee and to the Co-op.

The Investment Adviser has provided advice on an appropriate investment strategy with input from the Fund Actuary and the Co-op on the acceptable degree of mismatch between the assets and liabilities.

The current investment strategy as agreed by the Trustee is shown in the table below. The Trustee has agreed a new target investment strategy, which is also outlined in the table below. The Trustee has instructed one of the Fund's Illiquid Credit investment managers to enter 'run-off' naturally over time, which will result in the return of capital to the Trustee as investments are realised.

The Trustee has agreed that the proceeds from the redemption are to be invested equally into the existing Buy and Maintain portfolios, resulting in an increase to the strategic allocation to Investment Grade Credit and a reduction in the strategic allocation to Illiquid Credit. The new target investment strategy will take approximately 2-3 years to implement. The expected return is expected to remain broadly unchanged at gilts + 1.2% p.a.

<b>Asset Class</b>	<b>Current Allocation %</b>	<b>Target Allocation (%)</b>
Passive Global ESG Equity	7.0	7.0
Active Sustainable Global Equity	7.0	7.0
Illiquid Credit	10.0	6.7
Investment Grade Credit	40.0	43.3
Liability Driven Investments	36.0	36.0
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

The Trustee has agreed that rebalancing should occur on a pragmatic basis, whereby cashflows either into or out of the Fund will be used to broadly maintain the asset allocation in line with the target investment strategy noted above (albeit cashflows into / out of illiquid credit assets will be opportunity dependent). Market movements may mean that the actual allocation may deviate from that shown in the table above from time to time.

The overall asset allocation will be monitored on a quarterly basis via the strategic monitoring reports provided by the Investment Adviser. The Trustee's investment advisor will propose further rebalancing if deemed appropriate (particularly if the portfolio's long term expected return moves sufficiently far away from the required level).

## **7. *Expected Return***

The target excess return from the Fund's investment policy is 1.2% p.a. above a gilt based measure of the liabilities. (The actual expected excess return on the asset portfolio will vary with market movements and the underlying asset class assumptions, but the Trustee aims to maintain it broadly in line with the specified target over time.)

The Trustee expects that future investment returns will at least meet the rate of return required to fund the liabilities over the medium to long term, as assumed in the ongoing actuarial valuation.

## **8. *Day-to-Day Management of the Assets***

In compliance with the Financial Services and Markets Act 2000, day to day management of the assets is delegated to professional Investment Managers who are all regulated by the Financial Conduct Authority (“FCA”) or the relevant authority in the domicile country. The Investment Managers have full discretion to buy and sell investments on behalf of the Fund subject to the terms and conditions contained within the documentation governing their appointment.

## **9. *Investment Manager Appointment, Engagement and Monitoring***

### **9.1 *Aligning Manager Appointments with Investment Strategy***

When engaging with investment managers to implement the Trustee’s investment strategy, the Trustee believes that as appropriate and to the extent applicable its appointed investment managers should be incentivised to align their strategy and decisions with the objectives of the Fund.

Investment managers are appointed based on their capabilities and, therefore, the perceived likelihood of achieving the stated expected return risk characteristics required for the asset class they are selected to manage.

For the Fund’s investments that are made through pooled investment vehicles, the Trustee accepts that they have no ability to specify the stated risk profile and return targets of the manager for the pooled fund in which they invest. However, appropriate mandates can be selected to align with the Fund’s overall investment strategy.

For the Fund’s investments that are segregated, the Trustee has agreed criteria in the Investment Manager Agreements (“IMAs”) so that the assets are managed in line with the Trustee’s specific investment requirements.

With respect to the Liability Driven Investments portfolio, the manager has been appointed to manage the assets in line with a Fund-specific benchmark based on the liability profile, with restrictions set out in the IMA in order to manage portfolio-specific risks.

The Trustee utilises the Investment Adviser’s forward-looking assessment of a manager’s ability to outperform over a full market cycle. This view will be based on the Investment Adviser’s assessment of the manager’s idea generation, portfolio construction, implementation and business management, in relation to the particular investment fund that the Fund invests in. The Investment Adviser’s manager research ratings assist with due diligence and questioning managers during presentations to the Trustee (or the MMIC) and are used in decisions around selection, retention and realisation of manager appointments.

If the investment objective for a particular manager’s fund changes, the Trustee will review the fund appointment to ensure it remains appropriate and consistent with the wider Trustee investment objectives.

## 9.2 *Manager Appointments and Performance*

The Trustee receives, and considers, performance reports produced on a quarterly basis, which present performance information and commentary on the Funds they invest in over various time periods. The Trustee reviews the absolute performance and where relevant, will also consider relative performance against a suitable index used as the benchmark and/or against the manager's stated target performance (over the relevant time period) on a net of fees basis. In terms of reporting, the Trustee's focus is primarily on long term performance but short term performance is also reviewed.

The Trustee may review a manager's appointment if:

- There are sustained periods of underperformance;
- There is a change in the underlying objectives of the investment manager, or a change in the portfolio manager;
- There is a significant change to the Investment Adviser's rating of the manager; or
- There is a strategic change to the overall strategy that no longer requires exposure to that asset class or manager.

The majority of investment managers are remunerated by way of a fee calculated as a percentage of assets under management.

The investment managers are aware that their continued appointment is based on their success in delivering the mandate for which they have been appointed. If the Trustee is dissatisfied, then it may look to replace the manager or in some circumstances ask the manager to review the Annual Management Charge.

## 9.3 *Portfolio Turnover Costs*

The Trustee has engaged a third party to collect cost information (under the Cost Transparency Initiative). Once set up, the aim is for them to analyse data from the Fund's investment managers to determine the underlying costs involved with its investments. The Trustee aims to use this information to prompt discussion with its investment managers on costs and in order to compare its investments with other managers in the same asset class to ensure consistency.

The Trustee also receives portfolio turnover information for some of its mandates as part of the quarterly reporting provided by its Investment Adviser.

Investment manager performance is generally reported net of transaction costs (where possible), and therefore managers are incentivised in this way to keep portfolio turnover costs to the minimum required to meet or exceed their objectives.

The Trustee will continue to monitor industry improvements concerning the reporting of portfolio turnover costs.

#### **9.4 *Manager Turnover***

The Trustee is a long-term investor and is not looking to change the investment arrangements on a frequent basis. There is therefore no set duration for manager appointments. The Trustee typically expects to retain an investment manager unless:

- There is a change to the overall investment strategy that no longer requires exposure to that asset class or manager.
- The manager appointed has been reviewed and the Trustee has decided to terminate the mandate.

### **10. *Realisation of Investments***

The investment managers have discretion in the timing of realisation of investments and in considerations relating to the liquidity of those investments within parameters stipulated in the relevant appointment documentation.

The Trustee monitors the allocation between the appointed managers and between asset classes as appropriate. This includes consideration of the split within the broad asset classes shown above and the selection, monitoring and termination of the underlying investment managers.

### **11. *Additional Assets***

The Trustee is responsible for the investment arrangements of Additional Voluntary Contributions (“AVCs”) paid by members in the past and various immediate annuity contracts. The Trustee reviews the investment performance of the chosen AVC providers on a regular basis and takes advice as to the providers’ continued suitability.

### **12. *Socially Responsible Investment and Corporate Governance***

The Trustee has an RI Policy which it reviews at least annually. This document details the policy for considering ESG factors, including climate change, in the strategic investment process and investment decision making process, assessing the Fund’s investment managers’ performance on ESG issues, engagement with investee companies, consideration of and participation in third party ESG initiatives and public disclosure of the Fund’s RI Policy in practice.

In accordance with its fiduciary responsibilities, the Trustee takes account of financially material factors when making investment decisions, i.e. those factors which are expected to have an impact on investment returns and risk over the Fund’s anticipated lifetime (including the long-term sustainability of

investee companies' performance – in particular the impact of climate change).

The Trustee also recognises that it may take non-financial factors into consideration (i.e. those motivated by other concerns, such as social impact) where the Trustee has good reason to expect that Fund members would share these concerns, and where the decision is not expected to have material financial detriment.

The Trustee will apply these considerations in setting the RI Policy, with the Trustee assessing members' likely concerns (as far as this is practically possible) through engagement with members and through engagement with the Co-op when developing the Policy.

At the time of writing, the RI Policy reflects three broad Responsible Investment issues which the Trustee believes represent particular risk to the Fund and which the Trustee believes can be addressed. As the RI Policy is kept under regular review, the issues identified may change over time. These issues are:

- Protection of the environment.
- Labour conditions and equal pay.
- Corporate Governance.

The Trustee seeks to address these issues in a number of ways. For example, the Fund's equity assets are split between the LGIM Future World Funds which are managed on a passive basis and the Mirova Global Sustainable Equity fund which is managed on an active basis. The LGIM funds have tilts towards companies with positive ESG scores, as noted within Section 4. The Mirova mandate is actively managed and ESG principles are fully embedded within the investment process. In building the portfolio, there is a focus on thematic views, and Mirova's opinion on ESG risks and alerts on potential human rights breaches. The mandate has an implied temperature rise of 1.5 degrees which is consistent with a Net Zero 2050 objective in line with the Paris Agreement, with this metric approximately 2 degrees below the benchmark index.

The Trustee also applies a specific exclusion list of stocks for the segregated investment grade credit mandate to restrict investment in companies identified as conflicting with the Trustee's aims under these issues.

The Trustee gives its investment managers full discretion to evaluate ESG factors and engage with companies. The Trustee also encourages its investment managers to adopt best practices in these areas and to act in the best interests of Fund members. The Trustee recognises that where investments are held in pooled funds, it may not be possible to instruct the manager to follow a separate voting policy or to exercise votes. The Trustee may, from time to time, raise specific ESG issues with investment managers and seek a response.

Investment Managers are asked to report to the Investment Committee on the issue of Responsible Investment. In addition, the Investment Committee

monitors how each manager is incorporating ESG issues into investment decisions and, where relevant, exercising their approach to stewardship.

As part of the appointment of new investment managers and its ongoing monitoring process, the Trustee will consider the Investment Adviser's assessment (in terms of ESG ratings) of how each investment manager embeds ESG and stewardship factors into its investment process and how the manager's responsible investment philosophy aligns with the Trustee's Responsible Investment policy. This includes the investment managers' policy on voting and engagement.

While the Trustee or Investment Committee will meet with certain managers from time to time (including the LDI manager which the Fund's Investment Committee aims to meet at least annually), the MMIC is typically responsible for meeting with the Fund's investment managers. At any manager presentation, the MMIC on behalf of the Trustee will ask the investment managers to provide further detail about ESG considerations such as voting history, engagement activity and AAF reports.

In addition, the Trustee carries out regular reviews of the managers' ESG policies and actively engages with managers to better understand their processes.

The Fund's passive and active global equity managers are expected to report on their adherence to the UK Stewardship Code on an annual basis.

### **13. *Professional Investment Advice***

The Trustee has appointed Mercer Limited to provide advice on all aspects of investments relating to the Fund.

### **14. *Review of this Statement***

The Trustee will review this Statement annually and without delay after any significant change in investment policy. The Investment Adviser will provide the advice needed to allow the Trustee to review and update this Statement as required. In addition, no change will be made to the Statement unless the proposed changes to investment policy have been approved by the Trustee and recorded in the minutes of a Trustee meeting.

**Approved by TCG Northern Trustees Limited on 22 March 2022**

## Appendix: Division of Duties and Responsibilities

Duties and Responsibilities	Executed By
<ul style="list-style-type: none"> <li>▪ Overall responsibility for the Fund’s investments.</li> <li>▪ Define the terms of appointment of the Investment Committee.</li> <li>▪ Appoint the members of Investment Committee.</li> </ul>	The Trustee
<ul style="list-style-type: none"> <li>▪ Recommend the Investment Adviser to the Trustee.</li> <li>▪ Recommend investment objectives to the Trustee.</li> <li>▪ Recommend strategic framework to the Trustee.</li> <li>▪ Monitor the Investment Adviser and Investment Managers</li> <li>▪ Make day-to-day decisions relevant to the operation of the Fund’s investment strategy.</li> <li>▪ Review the Responsible Investment Policy and recommend possible changes to the Policy and to the Trustee (as appropriate).</li> </ul>	The Investment Committee
<ul style="list-style-type: none"> <li>▪ Monitor appointed Investment Managers and other service providers</li> </ul>	The Manager Monitoring and Implementation Committee
<ul style="list-style-type: none"> <li>▪ Perform asset liability modelling exercises, as required.</li> <li>▪ Advise on the strategic framework.</li> <li>▪ Advise on the selection of the Investment Managers.</li> <li>▪ Monitor the Investment Managers, providing both qualitative and quantitative input to the Investment Committee.</li> <li>▪ Advise on the implementation of mandates.</li> <li>▪ Advise on the Statement of Investment Principles.</li> </ul>	The Investment Adviser
<ul style="list-style-type: none"> <li>▪ Operate within the conditions set down by the Investment Management Agreement.</li> <li>▪ Select individual investments with regard to their suitability and diversification.</li> <li>▪ Supply the Trustee with sufficient information each quarter to allow the review of activity.</li> </ul>	The Investment Managers